NO. 144

IN THE

Supreme Court of the United States

OCTOBER TERM, 1961

STATE BOARD OF INSURANCE, ET AL., *Petitioners*

v.

TODD SHIPYARDS CORPORATION, *Respondent*

On Writ of Certiorari to the Court of Civil Appeals of Texas, Third Supreme Judicial District, Sitting in Austin, Texas

BRIEF FOR THE RESPONDENT

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STATEMENT OF THE CASE

Although substantially correct, the Petitioner's statement fails to correlate the facts with due process principles—"taxable event", location of the "taxable event", and the "nexus" between the "taxable event" and Texas.

1. The Taxable Event Is The "Purchase And The Premium Payment

Article 21.38(2)(e) defines the "taxable event":

> "Sec. 2. Tax on Insurance Premiums, . . .(e). . . If any . . . corporation shall *purchase* . . . (from an unadmitted insurer) . . . a policy of insurance covering risks within this state . . ., such corporation shall pay . . . a tax of 5% of the . . . *premiums paid* . . . Such tax shall be paid not later than thirty (30) days from the *date on which such premium is paid* to the unlicensed insurer." (Emphasis added)

The two indispensable elements in defining the "taxable event" are:

(1) The "purchase" of unadmitted insurance on Texas risks.

(2) The "payment" of the premiums.

The operating incidence of a similar tax is defined in *Compania General De Tabacos De Filipinas v. Collector of Internal Revenue*, 275 U.S. 87:

> "It is a tax on the contract or its proceeds which were not in the Philippines or expected to be there."

Although the "taxable event" may be argued to be the "purchase" of insurance measured by the "premium paid", the "taxable event" is the premium payment. If the premiums are not *paid*, no tax is levied—e.g., no tax is levied on uncollected open account sales. Moreover, the payment date is determined by the premium payment rather than the "purchase".

In a credit sale, there may be a "purchase", yet no tax. Payment is a sine qua non of the tax, and no premium may be paid without a tax; the premium payment is the "taxable event"—i.e., the transfer of money, New York property. Petitioner does not mention the "taxable event", but apparently concedes payment is the "taxable event" (Br. p. 3):

> " . . . *(the Act) levies a 5% tax on the gross premiums paid* . . ." (Emphasis added)

Without regard to whether the "taxable event" is the "purchase" or the "premium payment", the stipulation (R. 45) nonetheless conclusively establishes the "taxable event" occurred in New York with no Texas "nexus":

> "Each of the policies attached and made the basis of this suit was contracted for, delivered and paid for in the City of New York and State of New York, the domicile of Todd Shipyards Corporation."
>
> "All premiums are payable in New York City and have been paid in New York City."
>
> "Neither Lloyds of London nor the Institute of London Underwriters has ever solicited Todd's insurance business or policies within the State of Texas."
>
> "The Texas plants or offices of Todd Shipyards Corporation do not correspond directly or indirectly nor conduct any negotiations or transactions directly or indirectly with Lloyds of London or the Institute of London Underwriters, but all negotiations or transactions are handled by Todd's agent, Mr. Ed Costello, in New York City with the New York City Agents of the insurer or directly with the London office."

Petitioner concedes no Texas connection with the premium payment (R. 49, Stipulation, R. 186):

> "The premiums on each of the insurance policies are paid by and mailed from the Plaintiff's New York office to the New York office of the Broker. *No premium is paid by or from the Texas plants or offices.*" (Emphasis added)

Neither the measure nor the incidence of the tax is related to Texas transactions; Texas simply claims the power to tax Respondent's New York transactions. The operating incidence of the tax falls on Repondent's New York payment which has no reasonable relation to protection, opportunities and benefits afforded by Texas.

The "operating incidence" of the tax is on Respondent. Petitioner agrees (Br. p. 8):

> "Subsection (e) levies a tax *upon the insured* buying insurance for property or risks in Texas, so it is apparent that the tax is *not* placed on the unauthorized insurer." (Emphasis added)

Since the insurers are beyond the State's taxing talons, the operating incidence of the tax is imposed on Respondent.

2. The Tax Discriminates Against Unadmitted Insurers In Favor Of Texas Insurers

The stipulation (R. 46) clearly demonstrates the discrimination in favor of Texas insurers (R. 187):

> "The tax levied . . . on premiums paid . . . on policies purchased from . . . 'unadmitted insurers,' is at the rate of five per cent of the gross premiums. The tax on similar premiums paid to admitted insurers . . . is at rates of a maximum of 3.85%, to a minimum of 1.1%, Article 21.38, Texas Insurance Code and Article 7064, V.A.C.S."

In addition to the almost 500% discrimination in the tax rates (1.1% vs. 5%) in favor of Texas insurers, Article 7064 grants "admitted insurers" an additional sweeping tax exemption:

> "No occupation tax shall be levied on insurance companies herein subjected to the gross premium receipt tax by any county, city or town . . . The taxes aforesaid shall constitute all taxes collectible under the laws of this State against any such insurance carriers except maintenance taxes specially levied under the laws of this State and assessed by the Board of Insurance Commissioners. . . ."

This sweeping tax immunity further aggravates the rate discrimination. Respondent does not enjoy any similar tax immunity.

In spite of the plain words of Article 7064 to the contrary, the stipulation to the contrary (R. 46), and the State Court's clear holding to the contrary (Pet. C-7), Petitioner erroneously suggests (Br. p. 15) that Article 7064 levies a uniform 3.85% "premium tax" on authorized insurers. The tax ranges from 1.1% to 3.85% depending on the admitted insurer's investment in "Texas Securities". The scale discriminates in favor of Texas insurers and insurers investing in Texas.

In *Kansas City Title Insurance Co. v. Butler*, 253 S.W. 2d 318 (Ref. N.R.E.), the plain purpose of Article 7064 to discriminate in favor of Texas insurers is openly declared:

> "The act has for its purpose to encourage by offering a lower tax rate those insurance carriers subject to the Act to make investments in Texas securities and property in this State."

Petitioner's non-discriminatory argument is further refuted by Article 21.38(2)(c) providing in the plainest language for deliberate discrimination:

> "(c) When any policy of insurance . . . is procured under authority of such license, there shall be executed . . . an affidavit . . . showing that such insured was unable . . . to procure from any licensed company . . . the full amount of insurance required . . ., and further showing that the . . . insurance procured from non-licensed insurer . . . is *only the excess over the amount so procurable from licensed companies.*" (Emphasis added)

Furthermore, the premium tax on admitted insurers (Art. 7064) and the unadmitted tax paid to licensed agents (21.38 (2) (d)) allow a deduction for "return premiums". No deduction for return premiums is allowed in Article 21.38(2)(e). The patent discrimination accomplished by allowing a credit for return premiums in Article 7064 and Article 21.38 (2) (d), while denying a like credit to Respondent in Article 21.38 (2)(e), further establishes the discrimination.

Petitioner's non-discrimination argument contradicts its regulation argument. For example, in an effort to defend the tax as non-discriminatory, Petitioner states (Br. p. 15):

> "The tax levied by Article 21.38 (Section 2) was enacted to equalize the tax burden borne by Texas risks."

But, in its regulation argument, Petitioner (Br. p. 10) admits and, what is more, relies on the deliberate discrimination:

"Then, returning to the question, what is the regulatory effect of the tax levied by subsection (e), the simple effect of the tax is *to reduce the number* of owners of Texas risks *who purchase insurance from unauthorized companies by making it more expensive to do business with unauthorized insurance companies.*" (Emphasis added)

As Petitioner's regulation argument presupposes, the tax was plainly designed to make "it more expensive to do business with unauthorized insurance companies". This is deliberate discrimination. Petitioner's regulation arguments (Br. pp. 8-16) are each based on the premises that (1) insurance should be placed with regulated Texas insurers, (2) Texas may lawfully discriminate in favor of "Texas insurers", and (3) Texas has discriminated against the New York insurance in order to obtain a *"regulatory effect"*, to-wit, discourage New York insurance.

If Petitioner's non-discrimination arguments are accepted, the foundation for Petitioner's "regulation-nexus" arguments is destroyed. This is true, because any "regulatory effect" is wholly dependent on discriminatory rates. In other words, if the rates are not discriminatory, there is nothing to discourage New York insurance, and, consequently, no regulation.

In direct conflict with its argument that the tax was designed to *regulate* by unequal rates, Petitioner incongruously argues that the maintenance taxes levied on fire, casualty and compensation insurers equalize the tax. This is sophistry at its abysmal worst.

First, no compensation policies are in question, and Respondent's compensation is carried by an admitted insurer. Secondly, the casualty tax in Article 5.24 is levied at the rate of 2/5 of 1% of the premiums, and, to the limited

extent applicable to the policies of Respondent, would only slightly reduce the discrimination. Thirdly, only a small portion of Respondent's claim covers fire risk as defined in Article 5.49. This tax is levied at the rate of $1\frac{1}{4}\%$ and when added to the 1.1% minimum tax of Article 7064, would reduce the fire discrimination from 1.1% versus 5% to 2.35% versus 5%. Fourthly, the maintenance taxes are levied as a license fee for the privilege of doing a Texas insurance business, a privilege not extended to Repondent. Therefore, the maintenance taxes do not even reduce the discrimination against Respondent. A fortiori, no tax equalization is intended and none is accomplished by the maintenance taxes.

3. No "Minimal Contact" Or "Nexus" Exists

The "taxable event", the "purchase" of insurance and the "payment" of premiums, occurred solely in New York; therefore, Texas has no connection nor minimal contact with the "taxable event". Texas did not protect nor afford the opportunity to perform the "taxable event"; Texas offered the taxable transaction no protection nor benefit.

The connection to New York and Texas is best presented by comparison:

A. The New York Nexus:

(1) Respondent is a New York corporation domiciled in New York (R. 44-45).

(2) The insurers are domiciled in London, England (R. 45).

(3) Each policy was contracted for, delivered and paid for in New York (R. 45).

(4) Neither insurer conducts any investigation of Texas claims in Texas. The adjustment of losses is handled in New York between Respondent's agent and the insurer's agent (R. 45).

(5) Neither insurer has ever solicited Respondent's insurance business within the State of Texas (R. 45).

(6) Respondent's Texas plants do not correspond directly or indirectly or conduct any transactions or negotiations directly or indirectly with the insurers. All negotiations and transactions are handled by Respondent's New York agent, in New York, with the New York agents of the insurer or directly with the London office (R. 45).

(7) The following decisions relative to Respondent's insurance are made in New York, not in Texas: purchase, renewal, extent of coverage, amount of coverage, election of insurers and confirmation of insurance contracts (R. 45).

(8) All losses are payable and have been paid in New York (R. 45).

(9) All premiums are payable and have been paid in New York (R. 45).

(10) Respondent operates shipyards in New Jersey, Louisiana, California, Washington and South America, as well as in Texas (R. 46).

(11) Neither insurer has a permit from the Texas State Board of Insurance to write insurance in Texas (R. 47).

(12) Neither insurer submits any statement of its condition to the Texas State Board of Insurance (R. 47).

(13) None of the affairs of either insurer are in any way subject to examination by the Texas State Board of Insurance (R. 47).

(14) The Texas State Board of Insurance has no *Control Nor Supervision* over the affairs of either insurer (R. 47).

(15) At any time material to this suit, neither insurer had an office or agent in Texas (R. 47).

(16) None of the brokerage companies through whom such insurance is purchased for Respondent is located in Texas or is an insurance agent licensed under the law of the State of Texas (R. 48).

(17) All policies are signed in London, England (R. 48).

(18) All policies state that they are issued and delivered in London, but that between the insurer and insured, the place of issuance may be considered as New York (R. 48).

(19) All policies were accepted by Respondent in New York (R. 48).

(20) All policies are renewed by the payment of additional premiums in New York to the New York agents of the insurers (R. 48).

(21) Such renewals are negotiated in New York between the New York broker and Respondent's New York agent (R. 48).

(22) All premiums are paid in New York by Respondent's New York office to the New York office of the broker (R. 49).

(23) In the case of a builder's risk insurance, Respondent's New York agent applies in New York for such insurance (R. 49).

(24) After Respondent's New York agent is informed of a loss at one of Respondent's Texas plants, he notifies in New York the New York brokerage house that negotiated the insurance (R. 49).

(25) Such New York brokerage house appoints the London Salvage Association to prepare an estimate or "survey" of the Texas loss (R. 49).

(26) The London Salvage Association forwards its estimate of the Texas loss to Respondent's New York office (R. 49).

(27) London Salvage Association issues a bill to Respondent for services, and Respondent pays in New York (R. 49).

(28) The loss is adjusted in New York between the New York broker and Respondent's New York agent (R. 49, 50).

(29) The brokers who placed the insurance involved in this lawsuit are licensed in New York but not in Texas (R. 140, 48).

B. The Claimed Texas Nexus:

(1) Respondent is admitted to do business in Texas (R. 44).

(2) Respondent owns real and personal property in Texas (R. 44).

(3) The insurance covers "Texas Risks" (R. 44).

(4) Respondent had about 1500 employees in Texas in November, 1959 (R. 46).

(5) About 27% of Respondent's business was done in Texas in each of the years 1956, 1957, 1958 and 1959 (R. 46).

(6) In the case of builder's risk insurance, Respondent's Texas office notifies Respondent's New York agent that Respondent has entered into a construction or repair job (R. 49).

(7) Builder's risk insurance coverage is requested in the name of Todd's Texas division and identifies Texas as the place where the work is to be performed (R. 49).

(8) If a loss occurs at Respondent's Texas plants, the Texas plant notifies Respondent's New York agent of such loss (R. 49).

(9) The London Salvage Association appraises losses occurring at Respondent's Texas plants (R. 49).

(10) Respondent's Texas plants appraise their losses (R. 49).

(11) Respondent's Texas plants assist the London Salvage Association in arriving at a fair figure for the loss (R. 49).

None of Petitioner's claimed "nexus" facts are connected with the "taxable event"—"premium payment" and "purchase" of insurance.

Since Respondent is doing business in Texas, Respondent is subject to Texas jurisdiction. But, Texas may not tax Respondent's contracts, purchases and payments in New York—i.e., what Respondent does outside Texas. This case is entirely different from *Travelers H.A. v. Virginia*, 339 U.S. 643, evaluating a corporation's "nexus" in a doing business case. Respondent is admittedly doing business in Texas, but this does not furnish the "nexus" to tax Respondent's New York contracts, payments, properties or transfers.

The distinction in the "nexus" concept applicable to an admitted company is nicely drawn in *Connecticut General Life Insurance Company v. Johnson*, 303 U.S. 77:

> "Hence it is that a state which controls the property and activities within its boundaries of a foreign corporation admitted to do business there may tax them. But the due process clause denies to the state power to tax or regulate the corporation's property and activities elsewhere."

Johnson teaches that due process keeps Texas' taxing power at home; yet, this tax unlawfully extends the taxing grasp to New York. This is crystal-clear, because Petitioner concedes the "taxable event" occurred in New York.

4. The Unadmitted Insurance Tax Is An Occupation Tax And Not A Regulation

Although the state court properly ignores Petitioner's regulation argument, Petitioner insists the unadmitted in-

surance tax is a *"Regulation"* rather than a *"Tax"*. Yet, the constitutional effect of the "tax" cannot be changed by its characterization. This is the lesson of *St. Louis Cotton Compress Co. v. Arkansas*, 260 U.S. 346, 348:

> "The Supreme Court justified the imposition as an occupation tax,—that is, as we understand it, a tax upon the occupation of the defendant. But this court, although bound by the construction that the supreme court may put upon the statute, is not bound by the characterization of it, so far as that characterization may bear upon the question of its constitutional effect."

However, Petitioner's insistence that the "tax" is a "regulation" is devoid of merit. Shortly after the enactment of the tax in 1957, the State administrators determined that the tax is an *"Occupation Tax"* (R. 137, 38-43). Texas has set aside one-fourth of the tax to the public free school fund as required of all occupation taxes by Article VII, Section 3, of the *Texas Constitution*. This was done, because the administrators classified the tax as an occupation tax (R. 38-43). Although Petitioner argues regulation rather than taxation, the administrators deliberately found taxation rather than regulation. In light of the administrative finding, Petitioner's regulation argument is impotent.

Moreover, at the time of the tax's enactment, the Legislature expressly declared its purpose in Section 7 of Chapter 395 of the Laws of the Regular Session of the 55th Legislature as follows:

> "Sec. 7. The fact that the present laws relating to the placement of surplus lines of insurance do not provide adequately *for the conditions under which it*

> *shall be placed with unauthorized insurers in a manner which will insure the collection of the tax levied upon the premiums* charged or paid for such insurance creates an emergency and an imperative public necessity. . . ." (emphasis added)

In light of this openly avowed declaration of intention to insure collection of the *tax on premiums*—i.e., the collecting of the tax theretofore levied in Article 21.38(2)(d) and thereupon levied in Article 21.38(2)(e)—Petitioner's argument of a different intention is untenable. In other words, the 1957 amendment simply eliminated the only possibility—paying premiums directly to "unauthorized insurers"—for avoiding the discriminatory five per cent (5%) tax imposed by Article 21.38(2)(d) in 1951.

The Legislative purpose—to tax and to collect the tax, as a revenue measure—was carried into effect by the administrative construction. Any attempt to renounce the Legislature's avowed tax purpose is plainly without merit and an untimely afterthought induced by this case.

Petitioner's pretension that the tax is something else, regulation, is refuted by Petitioner's stipulation that neither of the insurers was subject to Texas regulation (R. 47). This is confirmed by the testimony of the administrator (R. 38):

> "Q. Do you do anything to try to regulate where or from whom Todd Shipyards buys its insurance?
> A. No, sir."

5. Respondent's Domicile Is New York

The Petition (p. 10) states, "Respondent is a Texas resident". Respondent does not know in what sense "resident" is used by Petitioner, but the stipulation (Tr. p. 46) conclusively establishes Respondent's domicile in New York:

> "Todd Shipyards has its principal office, principal place of business and domicile in New York City, New York."

Respondent is a resident of Texas only in the sense that each foreign corporation having a place of business and a permit to do business in Texas is a Texas resident. Therefore, Texas' jurisdiction to tax may not be sustained on the basis of a Texas domicile, as might be done in an intangible tax case; see *Kirtland v. Hotchkiss*, 100 U.S. 491; *Central Hanover Bank & Trust Company v. Kelly*, 319 U.S. 94.

6. Respondent Has Paid All Taxes Required For The Privilege Of Doing Business In Texas

Since 1934 Respondent has duly maintained its Texas "permit to do business" and has duly paid all taxes, fees and charges levied against Respondent for its Texas "permit to do business" and has duly paid all taxes, fees and charges levied against Respondent for the privilege of doing business in Texas (R. 46). Respondent was admitted for 23 years before the tax; Petitioner does not attempt to justify this tax as a tax for the granted privilege of doing business.

7. The Insurers Do Not Do Business In Texas

Petitioner concedes that the insurers are not admitted to do business in Texas and do not do business in Texas (R. 47). Respondent is in the ship repair, conversion and construction business, not the insurance business (R. 46-47).

8. The Trial Court's Constitutional Holding Is Not Limited To Due Process

Petitioner's Brief, page 3 states:

> "The Trial Court found the tax invalid as a violation of due process."

The judgment does not limit its findings of unconstitutionality to the due process point, but, on the other hand, broadly declares the tax unconstitutional without specifying the Texas or U. S. Constitutional ground (R. 179):

> " . . . Texas Insurance Code, Article 21.38(2)(e) is unconstitutional and void as applied to the . . . taxes unlawfully exacted from Plaintiff."

9. The Tax Applies Without Regard To Availability In Texas

The tax applies to unadmitted insurance whether available in Texas or not. Section (d) assumes some of the unadmitted insurance is not available in Texas by permitting a licensed broker to purchase in the unadmitted market, if, but only if, the insurance is not available in the admitted market.

The necessity of purchases in the unadmitted market rebuts Petitioner's economic and regulatory arguments. If Texas insurance is not available, the tax cannot coerce an impossible "admitted" purchase as contemplated by Petitioner's economic and regulatory arguments. In a nutshell, the failure to base the tax on Texas' availability precludes any regulatory or economic purpose.

Questions Presented

(1) Is the Texas unadmitted insurance tax levied on Respondent's New York contracts and premium payments unconstitutional under the due process clause of the U. S. Constitution's Fourteenth Amendment as held by the Texas courts on the authority of *St. Louis Cotton Compress Co. v. State of Arkansas*, 260 U.S. 346? Since Petitioner does not distinguish *St. Louis Compress*, the threshhold question is simply, "*should St. Louis Cotton Compress* be overruled?"

(2) Should this Court follow the law established and followed since 1896 in *Allgeyer*, *St. Louis Compress*, *Compania General De Tabacos De Filipinas*, and *Connecticut General Life Insurance Company*, because Respondent's business and the business of insurance have been "left for 65 years to develop, on the understanding" that Respondent was not obligated to pay the challenged tax?

(3) Is the arbitrary discrimination against unadmitted insurers and in favor of Texas insurers embodied in the tax unconstitutional under the equal protection clause of the U. S. Constitution's Fourteenth Amendment?

(4) Does the Court have jurisdiction, when the Texas Supreme Court may have rested its judgment upon an adequate State ground?

SUMMARY OF ARGUMENT

1. The Due Process Argument

A. The tax is condemned by due process of law because levied on a "taxable event" outside the state.

B. The tax is condemned by the *St. Louis Cottom Compress Co. v. State of Arkansas*, 260 U.S. 346; *Allgeyer v. Louisiana*, 165 U.S. 578; *Compania*, 275 U.S. 87, and *Connecticut General Life Insurance v. Johnson*, 303 U.S. 77.

C. *St. Louis Compress* should not be overruled.

(1) Petitioner's authorities do not conflict with *St. Louis Compress*.

(2) The *Tooison*, 346 U.S. 356, rule precludes overruling *St. Louis Compress*.

(3) *St. Louis Compress* should not be overruled, because its constitutional policy is sound.

(a) The states' taxing power must remain at home.

(b) Texas should not be permitted to tax or regulate the New York insurance market.

(c) If *St. Louis Compress* is overruled, the states will adopt conflicting regulations and taxation.

(4) *St. Louis Compress* is not dormant authority, but was recognized in March, 1960, in *Federal Trade Commission v. Travelers Health Association*, 362 U.S. 293, 301.

D. Texas does not have the "nexus" required to obtain jurisdiction to tax Respondent's New York contracts and premium payments.

(1) The "taxable event" has no connection with Texas.

E. Petitioner's jurisdiction to tax is not determined by discrimination.

2. The Equal Protection Argument

A. Article 21.38(2)(e) discriminates in favor of admitted insurers and against unadmitted insurers.

B. Equal protection condemns the state's attempt to favor admitted insurers and discriminate against unadmitted insurers.

(1) *Hanover Fire Insurance Company v. Carr*, 272 U.S. 494;
(2) *Wheeling Steel Corporation v. Glander*, 337 U.S. 562.

C. The exemption of admitted insurers from the tax denies equal protection.

(1) *Morey v. Doud*, 354 U.S. 457.

3. The Jurisdiction Question

A. The Texas Supreme Court may have rested its judgment on an adequate state ground, i.e., the tax violated the due process clause and the equality and uniformity clause of the Texas Constitution.

B. Therefore, the United States Supreme Court has no jurisdiction of this case. *Durley v. Mayo*, 351 U.S. 277.

Argument

1. Due Process Argument

Jurisdictional boundaries on the state's taxing power were drawn prior to due process. The limitation was originally expressed in terms of "fundamental law" and "lack of jurisdiction over the subject matter". See *Case of the State Tax on Foreign-Held Bonds*, 82 U.S. 300; *Northern Central Railway Co. v. Jackson*, 74 U.S. 262. Since the Fourteenth Amendment, the boundaries of the state's tax jurisdiction have been expressed in terms of due process. Although the boundary may be narrow, the challenged tax is condemned by an old, well defined, jurisdictional boundary. *Allgeyer v. Louisiana*, 165 U.S. 578; *St. Louis Cotton Compress Co. v. Arkansas*, 260 U.S. 346; *Compania General De Tobacos De Filipinas v. Collector of Internal Revenue*, 275 U.S. 87; *Connecticut General Life Insurance Co. v. Johnson*, 303 U.S. 77. The tax has been consistently condemned by constitutional policy since *Allgeyer*, 165 U.S. 578, in 1896.

A. The Tax Is Condemned By The St. Louis Cotton Compress Co. v. Arkansas, 260 U.S. 346 Line Of Cases.

As stated by the state courts (R. 190, 242), *St. Louis Cotton Compress Co. v. Arkansas*, 260 U.S. 346 is indistinguishable and invalidates the Texas tax. Moreover, Petitioner concedes *St. Louis Cotton Compress* is controlling, but argues it has been or, at least, should be "cast aside" (Br. p. 7).

The Stipulation (R. 41) establishes the *St. Louis Cotton Compress* facts set forth in a succinct opinion of Justice Holmes, as follows:

"This is a suit by the State of Arkansas against a corporation of Missouri *authorized to do business in* Arkansas. It is brought to recover 5 per cent on the gross premiums paid by the defendant, the plaintiff in error, for insurance *upon its property in Arkansas, to companies not authorized to do business in the State.* A statute of the state purports to impose a liability for this amount as a tax . . . The answer alleged that the policies *were contracted for, delivered, and paid for in St. Louis, Missouri,* the domicile of the corporation, because the rates were less than those charged by companies authorized to do business in Arkansas. It is also alleged that long before the taxing act was passed the defendant had made large investments in Arkansas in real and personal property essential to the conduct of its business, which it has held and operated ever since. . . .

" . . . *It is true that the state may regulate the activities of foreign corporations within the state, but it cannot regulate or interfere with what they do outside.*" (Emphasis added)

Respondent's position and the Texas tax are identical to *St. Louis Compress'* position and the Arkansas tax. Petitioner is simply at war with *St. Louis Compress.*

St. Louis Compress was reaffirmed in *Compania General De Tabacos De Filipinas v. Collector of Internal Revenue,* 275 U.S. 87, by condemning the tax on the extra-territorial premiums paid to an unadmitted insurer (Paris insurer) that could not be justified as a tax for the privilege of doing business; *Compania,* however, justified the same tax on extra-territorial premium payments to the admitted insurer (London insurer) as a tax on the privilege of doing business. Respondent is in the same position as the unadmitted (Paris) insurer in *Compania.* The Texas tax is

not for a privilege to do business, because (1) Petitioner concedes Respondent has paid all taxes for doing Texas business (R. 46), and (2) Respondent's insurers were not admitted and did not do business in Texas (R. 44-49).

Although due process was not controlling in *Compania*, the same principles were controlling. These principles are sharply defined:

> "The collection of this tax involves an exaction upon a company of Spain lawfully doing business in the Phillippine Islands effected by reason of a contract made by that company with a company in Paris on merchandise shipped from the Philippine Islands for delivery in Barcelona. It is an imposition upon a contract not made in the Philippines and having no situs there and to be measured by money paid as premium in Paris, with the place of payment of loss, if any, in Paris. We are very clear that the contract and the premiums paid under it are not within the jurisdiction of the government of the Philippine Islands."

The Texas tax is on a contract and payment not made in Texas—no Texas situs—with the place of payment of loss, if any, in New York. As stated in *Compania*, the contract and the premiums paid were not within the jurisdiction of Texas.

Compania draws a jurisdictional boundary placing payment to admitted companies *(Compania's* London insurer) inside and to unadmitted companies *(St. Louis Compress)* outside the boundary on substantially identical transactions. This boundary may be narrow, but "a boundary line is none the worse for being narrow".

Connecticut General Life Insurance Co. v. Johnson, 303 U.S. 77, condemns a California tax on premiums paid to

an admitted insurer in Connecticut on Connecticut contracts. The premiums were paid and the losses were payable in Connecticut. The jurisdictional boundary is correctly defined:

> "But the limits of the state's legislative jurisdiction to tax, prescribed by the Fourteenth Amendment, are to be ascertained *by reference to the incidence of the tax upon its objects rather than the ultimate thrust of the economic benefits and burdens of transactions within the state. As a matter of convenience and certainty, and to secure a practically just operation of the constitutional prohibition, we look to the state power to control the objects of the tax as marking the boundaries of the power to lay it.* Hence it is that a state which controls the property and activities within its boundaries of a foreign corporation admitted to do business there may tax them. *But the due process clause denies to the state power to tax or regulate the corporation's property and activities elsewhere. . . .*"
>
> "Appellant, by its reinsurance contracts, undertook only to indemnify the insured companies against loss upon their policies written in California. The reinsurance involved no transactions or relationship between appellant and those originally insured, and called for no act in California. . . . Apart from the facts that appellant was privileged *to do business in California*, and that the risks reinsured were originally insured against in that state by companies also authorized to do business there, California has no relationship to appellant or to the reinsurance contracts. *No act in the course of their formation, performance or discharge, took place there. The performance of those acts was not dependent upon any privilege or authority granted by it, and California laws afforded to them no protection.*"

". . . All that appellant did in effecting the reinsurance was done without the state *and for its transaction no privilege or license by California was needful.* The tax cannot be sustained either as laid on property, business done, or transactions carried on within the state, or as a tax on a privilege granted by the state." (Emphasis added)

Johnson also squarely condemns Texas' attempt to levy an extra-territorial tax on Respondent. Respondent's position is stronger than in *Johnson,* since (1) the *Johnson* insurer was doing business in the taxing jurisdiction, and (2) if continued in effect, losses on a *Johnson* life policy were inevitable, while Respondent's losses are not inevitable but controlled by chance phenomena.

The same boundary is drawn in *Allgeyer v. Louisiana,* 165 U.S. 578, condemning a fine imposed for insuring with unauthorized insurers.

B. St. Louis Compress And Its Progeny Should Not Be Overruled.

Petitioner does not attempt to distinguish *Allgeyer, St. Louis Compress, Compania* or *Connecticut General,* but, nevertheless, insists that, although controlling, they are "repudiated" by current policy and should, therefore, be overruled.

In the first place, Petitioner's authorities do not conflict with *St. Louis Compress.* Petitioner's reliance on conflict with *Osborn v. Ozlin,* 310 U.S. 53, and similar cases, is misplaced. In *Osborn* the Virginia statute provided that no insurance on Viriginia property should be issued by an admitted company unless countersigned by a resident agent who was forbidden to share more than 50% of his commission with non-resident brokers; the Court held that

since (1) the statute was applicable only to admitted companies, and thus, within the granted privilege, and (2) the statute was not aimed at contracts beyond Virginia's borders, due process was not denied. *Osborn* specifically distinguishes *St. Louis Compress Co.*, *Compania* and *Allgeyer* on the basis that *Allgeyer*, *St. Louis Compress* and *Compania* (1) were not directed at the regulation of insurance within the state, but to the making of contracts outside the state, and (2) the *St. Louis Compress* tax was not for a granted privilege.

Since *Osborn* carefully distinguishes *St. Louis Compress*, *Osborn* is no authority for overruling *St. Louis Compress*. Moreover, *Osborn* does not uphold any tax, much less an extra-territorial tax, and holds nothing on a state's extra-territorial taxing power.

Petitioner also relies on *Hoopeston Canning Co. v. Cullen*, 318 U.S. 313, upholding New York's right to regulate an admitted insurer as a condition to admission. The *Allgeyer* and *St. Louis Compress* rule is distinguished in *Hoopeston Canning Co.*, and, therefore, *Hoopeston* cannot justify overruling *St. Louis Compress*. Furthermore, *Hoopeston* is not a tax case with an extra-territorial "taxable event".

Travelers Health Association v. Virginia, 339 U.S. 643, (1) is not a tax case, (2) does not overrule *St. Louis Compress*, (3) upholds state jurisdiction of an insurer doing business within the state, (4) upholds substituted service, and (5) holds nothing on extra-territorial transactions. *Travelers Health Association* is not in point. The opinion correctly points out that *Osborn*, *Hoopeston* and *Travelers* do not conflict with *Allgeyer*, 339 U.S. 650:

> ". . . Hoopeston Canning Co. v. Cullen, supra, 318 U.S. 320, 321, 87 L. Ed. 784, 785, 63 S. Ct. 602, 145

ALR 1115). See also Osborn v. Ozlin, 310 U.S. 53, 62 L. Ed. 1074, 1077, 60 S. Ct. 758. These two opinions make clear that Allgeyer v. Louisiana, 165 U.S. 578, 41 L. Ed. 832, 17 S. Ct. 427, requires no different result."

Watson v. Employers Liability Assurance Corporation, 348 US. 66, upholds a "direct action" statute against an admitted insurer. No extra-territorial transaction was presented by *Watson*. *Watson* does not conflict with *St. Louis Compress* as noted in the concurring opinion, 348 U.S. 66, 83. *Watson* does not justify overruling *St. Louis Compress*.

In the second place, *St. Louis Compress* and its progeny trace their origin to the 1896 *Allgeyer* decision. For more than 65 years the insurance and Respondent's businesses have been "left to develop" on the understanding that constitutional policy precludes the challenged tax. Moreover, Respondent entered Texas in 1934, made large investments in Texas and developed its Texas business for more than 23 years on the understanding that Respondent was not subject to the tax.

Toolson v. New York Yankees, Inc., 346 U.S. 356, holds a statutory policy of 30 years should not be overruled, because the business of baseball had been "left for 30 years to develop" on the understanding that it was not subject to existing anti-trust legislation. In a short opinion, the court squarely holds that the law should not be re-examined, if a business has been permitted to develop in reliance on a prior, long-standing decision:

> "In Federal Baseball Club of Baltimore v. National League of Professional Baseball Clubs, 259 U.S. 200, 66 L. Ed. 898, 42 S. Ct. 465, 26 ALR 257 (1922),

this Court held that the business of providing public baseball games for profits between clubs of professional baseball players was not within the scope of the federal antitrust laws. Congress has had the ruling under consideration but has not seen fit to bring such business under these laws by legislation having prospective effect. The business has thus been left for thirty years to develop, on the understanding that it was not subject to existing anti-trust legislation. The present cases ask us to overrule the prior decision and, with retrospective effect, hold the legislation applicable. We think that if there are evils in this field which now warrant application to it of the anti-trust laws it should be by legislation. Without re-examination of the underlying issues, the judgments below are affirmed."

Toolson should be applied to constitutional as well as statutory policy. This is especially true, because the Congress may not have pre-empted this area in reliance on *St. Louis Compress.* For example, after the *Southeastern Underwriters* decision in 1945 in a committee report on the McCarran-Ferguson Act, the Congressional intention and reliance on *St. Louis Compress* was plainly recorded:

> "It is not the intention of Congress in the enactment of this legislation to clothe the States with any power to regulate or tax the business of insurance beyond that which they had been held to possess prior to the decision of the United States Supreme Court in the *Southeastern Underwriters Association* case. Briefly, your committee is of the opinion that we should provide for the continued regulation and taxation of insurance by the states, subject always, however, to the limitations set out in the controlling decisions of the United States Supreme Court, as, for instance, in *Allgeyer v. Louisiana* (165 U.S. 578),

> *St. Louis Cotton Compress Co. v. Arkansas* (260 U.S. 346) and *Connecticut General Life Insurance Co. v. Johnson*, (303 U.S. 77), which hold, inter alia, that *a State does not have power to tax contracts of insurance or reinsurance entered into outside its jurisdiction by individuals or corporations resident or domiciled therein covering risks within the State or to regulate such transactions in any way.*" (H.R. Rep. No. 143, 79th Congress, 1st Sess. 3).

The Congressional reliance on the *St. Louis Compress* line of authority confirms the soundness of *Toolson* when applied to constitutional policy. This Congressional intention was quoted and the policy approved in *Federal Trade Commission v. Travelers Health Association*, 362 U.S. 293, 301. Not only have the insurance and Respondent's businesses been left to develop in reliance on the understanding that *St. Louis Compress* expressed constitutional policy, the Congress was left to develop the relation between the State and Federal governments (pre-emption vel non) on the same understanding.

In light of the development of the insurance and Respondent's businesses plus Congressional reliance in adopting the McCarran-Ferguson Act, the *Toolson* rule should be followed, and *St. Louis Compress* should not be overruled.

In the third place, the *St. Louis Compress* constitutional policy is sound. The policy is aimed primarily at keeping the state's taxing power at home and avoiding conflicts between state laws. If Petitioner's proposal to permit Texas to tax New York contracts is adopted, a conflict in the laws of the two states may soon develop in an unseemly struggle by each state to favor its own. New York's power to regulate New York contracts could not reasonably be denied. A conflict may easily arise by conflicting "reserve

requirements" or conflicting "investment restrictions"; in the event of conflict, which state law would control? To which state would belong the coveted power to pre-empt the regulatory field? The point Respondent makes is that, if *St. Louis Compress* is overruled, the constitutional relationship among the states will be drastically affected by the opportunity to adopt conflicting regulation.

If the states of New York and Texas are each permitted to tax the same premium payments, there will inevitably result, not only double, if not multiple, taxation among the states, but an unseemly race among the states to gain new tax sources by contriving to tax extra-territorial transactions. If Texas is allowed to tax New York premium payments, Texas' taxing power will be released to roam unconfined and vagrant on property, transactions, occupations and business done in other states. This will not do, if the dual federal system is to survive.

In order to justify reshaping the historical boundary established in *St. Louis Compress*, Petitioner is content to rely on one and only one policy argument, to-wit: the State's interest in regulating or discouraging the placing of unadmitted insurance. The short answer is that (1) the "admitted insurance" market cannot and does not offer all of the coverage required by Respondent, and Respondent's resort to the New York market is necessary, whether discouraged or not, (2) the tax is levied (Article 21.38(2)(e)) without regard to whether admitted insurance is available or not, and (3) Texas' interest, however great, cannot reasonably be permitted to regulate or tax the New York insurance market.

Judge Holmes' genius for condensation permitted this policy to be reduced to a few words (260 U.S. 346).

"It is true that the state may regulate the activities of foreign corporations within the state, but it cannot regulate or interfere with what they do outside."

Article 21.38(2)(c) and (e) impose the tax, whether the insurance is available in Texas or not, and, therefore, provide in clearest language for extension of the Texas taxing arm to the New York insurance market. The New York insurance market should not be made vulnerable to Texas control.

C. St. Louis Compress Is Not Dormant Authority.

As late as 1960, the authority of *St. Louis Compress* and *Connecticut General Life Insurance Company* was recognized in *Federal Trade Commission v. Travelers Health Association*, 362 U.S. 293, 301.

D. Texas Does Not Have The "Nexus" Required To Obtain Jurisdiction To Tax Respondent's New York Contracts And Premium Payments.

Petitioner does not employ the conventional due process jurisdictional words of art, "nexus", "connection" or "minimal contact", but, perhaps, is saying the same thing by referring to the "interest of Texas". For example, Petitioner's Brief, page 10, characterizes the jurisdictional connection in this manner:

"Since the validity of subsection (e) must be determined by the *'degree of interest of Texas'* in the insurance contracts, it is then important to examine the interest of Texas in this insurance. . . ."

Each of Petitioner's "nexus" or "interest of Texas" arguments has been fully answered in the *St. Louis Com-*

press line of authority. In *St. Louis Compress*, the "nexus" argument was tersely refuted (260 U.S. 349):

> "The case is stronger that that of Allgeyer in that here no act was done within the state, whereas, there a letter constituting a step in the contract was posted within the jurisdiction. It is true that the state may regulate the activities of foreign corporations within the state, but it cannot regulate or interfere with what they do outside."

Petitioner's stipulation (R. 44-48) concedes no act relating to the insurance purchase, contract or premium payment was done in Texas. Therefore, no part of the "taxable event" was done in Texas. The stipulation tracks the language of *St. Louis Compress*, 260 U.S. 346, and *Johnson*, 303 U.S. 77.

In *Compania*, 275 U.S. 87, Petitioner's "nexus" argument based on the Texas location of the insured property is deliberately rejected:

> "But such reference can not be made a basis for an argument that such protection as the government of the Philippine Islands gave to the merchandise while being shipped at Manila furnished any jurisdiction for a tax by that Government on the premium paid in Barcelona upon the insurance contract. If that were to be admitted, then neither the Allgeyer nor the St. Louis Cotton Compress Co. Case could be sustained, *for the property in each of those cases was protected by the government seeking to impose the forbidden exactions upon the owner who obtained the insurance out of the state on that property within it. The tax here is not on the property insured.* It is a tax on the contract or its proceeds which were not in the Philippines or expected to be there." (Emphasis added)

Petitioner's situs of the risk argument is squarely rejected in *Allgeyer, St. Louis Compress, Compania* and *Johnson.*

Most of Petitioner's "nexus" arguments are based on the Texas location of the property insured, but, as held in *Compania*, the tax is not on the property. Rather, the tax is on the contract and the premiums which were never in Texas. The distinction between a tax on Texas property, and the tax on the New York contract or premium payment is decisive. This is especially true, since (1) Petitioner admits Respondent's payment of all property taxes, and (2) the tax is not based on property but solely on the admitted or unadmitted status of the insurer.

In *Johnson*, 303 U.S. 77, the state's interest in the lives of its residents was rejected as a jurisdictional "nexus". In *Johnson*, the Connecticut reinsurance contracts related to California contracts insuring the lives of California residents. But, the California insureds and contracts were held not to be a sufficient jurisdictional "nexus" to give California jurisdiction to tax the Connecticut reinsurance contract. Yet, *Johnson* presents a stronger jurisdictional "nexus' than is available to Petitioner, for (1) the state's relative interest in lives and property preponderates in favor of the lives in *Johnson*, and (2) the insurer was admitted.

Petitioner's economic arguments imagining the possibly dire economic consequences of a failure to pay a large loss, if it ever happens, are squarely rejected in *Johnson*, 303 U.S. 77, 80:

> "But the limits of the state's legislative jurisdiction to tax, prescribed by the Fourteenth Amendment, are to be ascertained by reference to the incidence of

> the tax upon its objects rather than the *ultimate thrust of the economic benefits and burdens of transactions within the state.*" (Emphasis added)

Jurisdiction to tax may not be predicated on the "ultimate thrust" of economic benefits and burdens of insurance and possible losses, if occurring, in the state. Neither may jurisdictional nexus be established by chimerical, economic consequences that have never happened and may never happen.

Jurisdictional "nexus" may not reasonably be based on vagrant conjectures of "possible" economic catastrophe superimposed on Petitioner's fanciful visions of possible future, fortuitous losses rather than existing facts or probabilities. For example, Petitioner's economic arguments are wholly conditioned on imagined, fortuitous, possible, future circumstances, to-wit:

(1) If Respondent has a large loss.

(2) If the insurers fail to pay the losses; yet Petitioner offers no evidence to support this possibility, although Respondent has purchased similar insurance from these insurers since 1934 (R. 48).

(3) If the insurers fail to pay, and if Respondent is unable to replace any future loss from its own resources.

A jurisdictional connection may not be based on imagined, fortuitous, speculative, economic effects of possible, future, fortuitous events that may never come to pass. Nexus must be based on existing "taxable events". If Petitioner's economic arguments are carried to their logical conclusion, Petitioner has a sufficient nexus with

the insurance of New York or California risks in New York, since, under some hypothetical chain of events or nuclear war imagined by Petitioner, a New York or California loss may possibly impair Respondent's capital and, thereby adversely affect its Texas business and employees.

Petitioner's economic and regulation arguments erroneously assume the taxed insurance is available from Texas insurers. This is true as to some but not all of Respondent's insurance; some of the insurance is not available from Texas insurers. As to the insurance unavailable in Texas, Petitioner's economic and regulation arguments are plainly specious; the state could hardly deny that Respondent, the economy and the "Texas interests" are better protected with unadmitted insurance than none and are better protected with unregulated insurance than none. The tax (Article 21.38(2)(e)) is not conditioned on the availability of admitted insurance. Moreover, Article 21.38 (2)(c), as well as section (e), deliberately imposes the tax even though the insurance is not available in Texas.

E. Petitioner's Jurisdiction To Tax Is Not Determined By Discrimination.

Although *St. Louis Cotton Compress*, 260 U.S. 346, invalidated a discriminatory tax, *Compania*, 275 U.S. 87, teaches that discrimination is not indispensable to the *St. Louis Cotton Compress* rule. The *Compania* opinion makes this crystal-clear, 275 U.S. 95:

> "Reference was made in the St. Louis Cotton Compress Co. Case to the fact that that which was imposed was larger than would have been the tax in the state if all parties had been in the state and the con-

> tract had been made there, but the decision itself clearly does not depend for its basis upon discrimination as between a tax and a prohibition or the amount of it."

However, the tax plainly subjects contracts with unadmitted insurers to discriminatory rates favoring admitted insurers. (Compare Article 21.38(2)(e), *Insurance Code* with Article 7064). Respondent's discrimination argument is addressed to the "equality" rather than the "due process" question.

F. The Tax Is Not Levied On Losses, But The Losses, If Occurring, Are Adjusted And Paid In New York.

The tax is not levied on insurance "losses" nor the adjusting of "losses" but is levied on the contract and premium payment without regard to "losses". Petitioner may not sustain the tax as a tax on "losses" that may or may not occur in the future; its arguments based on Texas' connection with "losses", if any, are patently specious. The same "loss nexus" was present in each of the *St. Louis Cotton Compress* lines of authority. "Losses" are adjusted and paid in New York (R. 49-50).

The only loss in the record (R. 134-135) was appraised in South Carolina by a Florida appraiser. This was under a Houston, Texas "builder's risk" policy, and Texas had absolutely no connection with the loss or its appraisal. As demonstrated by this loss, if Texas has a connection with a builder's risk loss, it is solely by chance. The requisite jurisdictional nexus may not be based on such chance phenomena—i.e.—(1) the chance a loss will occur, and (2) the chance the loss will be appraised in Texas.

G. The Tax Is Not In Return For Respondent's Privilege To Do Business In Texas.

Petitioner admits Respondent paid all of the taxes required for its privilege to do business in Texas (R. 46). Therefore, Petitioner concedes the "nexus" is not any privilege granted Respondent by the State.

H. The Nexus Must Relate To The "Taxable Event."

The requisite jurisdictional "nexus" must relate to the "taxable event" or the "taxable transaction"—Respondent's contract or the premium payment. Petitioner concedes the "taxable transaction" has no connection with Texas (R. 44-48). See *McLeod v. Dilworth*, 322 U.S. 327, a commerce clause, sales tax case, emphasizing and turning on the situs of the "taxable event".

I. The Notification Of Respondent's New York Office Of The Making Of Ship Repair Contracts Is Not A Sufficient Nexus With The Builder's Risk Insurance.

This notification (R. 49) extends only to the builder's risk insurance. The insufficiency of this nexus is clearly within the holding of *Compania*, 275 U.S. 87, 89, where the same basic law existed:

> "Subsequent to the purchase of the merchandise, the Tobacco Company from time to time shipped it to Europe, and *by cable notified its head office in Barcelona of the value of the shipments. The head office thereupon insured with the Paris Company. . . .*" (emphasis added)

J. The State's Power To Control The Objects Of The Tax Mark The Boundary Of The State's Jurisdiction To Tax.

In *Johnson*, 303 U.S. 77, the limits of the state's jurisdiction to tax is defined in terms of the state's right to control the objects of the tax, 303 U.S. 80:

> "As a matter of convenience and certainty, and to secure a practically just operation of the constitutional prohibition, we look to the state power to control the objects of the tax as marking the boundaries of the power to lay it."

In the face of transgressing this plain, jurisdictional boundary—i.e., the state's jurisdiction is limited to objects under its control—the state, nonetheless, frankly concedes that Texas has no supervision nor control over the insurance contracts (R. 44-47). Petitioner's regulation arguments are premised on its admitted inability to control the insurance contracts. This being true, the state has no jurisdiction to tax the contracts and payments which are beyond the state's power to control.

Apart from Respondent's Texas privilege to do business and the Texas location of the insured property, Texas has no connection with the taxed contracts or premium payments. No act in the making of the premium payments or the contracts took place in Texas. Respondent's making of the New York contracts and premium payments were not dependent on authority granted by Texas and were not afforded any protection by Texas. Texas may not withdraw nor impair Respondent's privilege of doing business in New York under the guise of either regulation or taxation. All that Respondent did was done in New York, and Respondent needed no Texas license. The tax cannot

be sustained as a tax on property, business done or transactions carried on in Texas. Neither may the tax be sustained as a tax on a privilege granted by the state. Therefore, the judgment invalidating the tax should be affirmed.

2. Equal Protection Argument

At the outset, Petitioner's argument that Respondent may not complain of the constitutionally unequal classification of insurers—admitted—unadmitted—, must be fairly met. Petitioner furnishes the basic premise (Br. p. 8):

> "*Subsection (e) levies a tax upon the insured buying insurance for property or risks in Texas, so it is apparent that the tax is not placed on the unauthorized insurer.*" (Emphasis added)

The burden of the tax is unequivocally imposed on Respondent who is the target of the classification. The arbitrary classification was adopted to reach and affect Respondent's class and no other class. Yet, Petitioner argues the insurers—who are not affected—rather than Respondent—who is adversely affected—are the only persons who may challenge the classification. If the taxpayer cannot challenge the unlawful tax, Respondent may look for protection only to a disinterested insurer. Respondent may not be left without a practical remedy unless, by chance, a disinterested insurer vicariously protects its interest.

In a nutshell, the tax is levied on the person paying premiums to the defined insurer class rather than directly on the insurer class; yet, the taxable classification is nevertheless based solely on the insurer's admitted or unadmitted status. *Phillips Chemical Co. v. Dumas Independent School District*, 361 U.S. 376, upholds a lessee of the United

States in an attack upon a discrimination against those dealing with the United States. *Phillips Chemical* teaches that Respondent may attack the unequal classification, since it deals with and is affected by the discriminatory classification.

A. The Rate Discrimination And Intention To Discriminate Against Unadmitted Insurers Is Plain.

Petitioner does not really argue that the statute is non-discriminatory (Br. p. 10):

> " . . . (e), the simple effect of the tax is to reduce the number . . . who purchase insurance from unauthorized companies by making it more expensive to do business with unauthorized insurance companies."

Article 21.38(2)(c) establishes the discriminatory purpose by requiring inability to obtain admitted insurance as a condition to buying in the unadmitted market. See Article 21.38(2)(c):

> "(c) When any policy of insurance or certificate of insurance is procured under authority of such license, there shall be executed by the insured an affidavit setting forth facts showing that such insured was unable after diligent effort to procure from any licensed company or companies the full amount of insurance required to protect the property, liability or risk desired to be insured, and further showing that the amount of insurance procured from nonlicensed insurer or insurers is only the excess over the amount so procurable from licensed companies."

The discriminatory rates, unequal treatment of return premiums, unequal grants of tax immunity, and the de-

liberate attempt to favor admitted insurers is fully set forth in the Statement of the Case.

B. Equal Protection Condemns The State's Attempt To Favor Domestic Insurers And Discriminate Against Foreign Insurers.

The unconstitutionality of a discrimination favoring domestic over foreign insurers has been well established since *Hanover Fire Insurance Company v. Carr*, 272 U.S. 494, invalidating under the equal protection clause, an Illinois net receipts tax levied on foreign corporations but exempting domestic corporations. The opinion tersely condemns the foreign-domestication corporation classification:

> "But an occupation tax imposed upon 100 percent of the net receipts of foreign insurance companies admitted to do business in Illinois *is a heavy discrimination in favor of domestic insurance companies of the same class and in the same business*, which pay only a tax on the assessment of personal property at a valuation reduced to one-half of 60 per cent of the full value of the property. It is a denial of the equal protection of the law." (Emphasis added)

Hanover Fire teaches that "Equal Protection" condemns taxes that favors domestic insurers and discriminate against foreign insurers.

The Court has uniformly condemned as constitutionally "unequal" all attempts by the states to favor transactions with *residents* and to discriminate against transactions with *non-residents*. The leading case is *Wheeling Steel Corporation v. Glander*, 337 U.S. 562, holding a tax on intangibles of a foreign corporation, although exempting identical in-

tangibles of residents, is an unconstitutional classification. *Glander* plainly declares that state taxation may not establish classifications to *favor residents* and to *discriminate against non-residents*.

The Court said:

> "It seems obvious that appellants are not accorded equal treatment, and the inequality is not because of the slightest difference in Ohio's relation to the decisive transaction, but *solely because of the different residence of the owner*." (Emphasis added)

Respondent is not accorded equal treatment and the inequality is not because of the slightest difference in Texas' relation to the premium payment, but the inequality is solely because of paying premiums to "unadmitted" insurers. The inequality deliberately favors Texas insurers and deliberately discriminates against the New York insurance market.

Glander teaches that (1) a state tax must equally apply to its residents and a foreign corporation, and (2) "Equal Protection" denies the states the right to favor their residents over non-residents. The Texas unadmitted insurance tax does not apply equally to admitted (residents) and unadmitted insurers (non-residents) and falls within the constitutional policy of *Glander*.

A more recent case, *Allied Stores of Ohio v. Bowers*, 358 U.S. 522, upheld an Ohio tax favoring property of non-residents and discriminating against property of residents. Yet, the concurring opinion carefully preserves *Glander's* authority and declares that any attempt to favor residents is "mechanically" condemned, i.e., discrimination in favor of residents is unlawful. The concurring opinion states:

> "There is, therefore, no reason to judge the state action mechanically by the same principles as state efforts to favor residents."

The Texas tax may be condemned "mechanically", because the tax is a clear effort to favor residents and "those paying tribute to the state".

Although the Court has approved many different schemes of classification and has approved a classification favoring non-residents over residents, the Court has uniformly condemned all attempts by states to levy taxes discriminating in favor of domestic corporation and discriminating against foreign corporations.

The point Respondent makes is that equal protection prevents a classification in favor of admitted and discriminating against unadmitted insurers. To state the point in yet another way, a classification of admitted and unadmitted insurers so as to favor the admitted insurers is an arbitrary and unconstitutionally unequal classification.

It is true that the tax accomplishes its intended discrimination by distinguishing between "admitted" and "unadmitted" insurers and does not expressly base the discrimination on residence and non-residence or on domestic and foreign insurers. No constitutionally relevant distinction may be made between the classification of "admitted and unadmitted insurers" and the classification of domestic and foreign insurers in *Hanover Fire*. Texas' effort to favor admitted and to discriminate against unadmitted insurers has the same vices as discrimination in favor of domestic over foreign insurers. Each of these discriminations permits the state to favor its own and is condemned by "Equal Protection".

The following classifications are constitutionally unequal:

(1) Domestic-Foreign Corporation classification favoring domestic corporation (*Hanover Fire*, *Glander*).

(2) Admitted—Unadmitted Insurance Company classification favoring admitted insurers, which is merely another way of favoring domestic insurers over foreign insurers.

C. The Exemption Of Domestic Insurers From The Tax Denies Equal Protection.

The Texas taxable event is the *payment of premiums* on Texas risks. All persons paying premiums on Texas risks to admitted insurers are exempt. The arbitrary exemption of payments to admitted insurers renders the tax unconstitutionally unequal. This "no-exemption" principle was followed in *Morey v. Doud*, 354 U.S. 457 when an Illinois license and regulatory statute applying to firms "selling or issuing money orders"—but exempting the American Express Company—was condemned as a denial of "Equal Protection".

In other words, after Illinois decided to regulate the "Selling and issuing of money orders" all people so selling and issuing are required by "Equal Protection" to be treated equally.

The *Morey* principle requires that all persons "paying premiums on Texas risks" be taxed equally and condemns the attempted Texas exemption in favor of payments to domestic insurers.

In a nutshell, Respondent's equality arguments are two-pronged:

(a) First:—Although the State may reasonably classify taxable events (premium payments on Texas risks), the State may not classify the persons performing the taxable event ("persons paying to admitted or unadmitted insurer"). The classification of persons renders the tax constitutionally unequal.

(b) Second:—Even though the State has the right to classify persons paying the taxed premiums, nevertheless, the attempted discriminatory classification in favor of payments to admitted insurers and against unadmitted insurers is constitutionally unequal.

The distinction between (a) and (b) is not always clearly drawn, yet Respondent submits that two "equality" questions are presented:

(1) The right to classify persons paying premiums on Texas risks, vel non, and

(2) The reasonableness of the classification—admitted and unadmitted insurers.

3. The Jurisdiction Question

The Petitioner's Application for Writ of Error in the Texas Supreme Court assigned, among others, the following errors (R. 194, 195).

POINT II.

"The Court of Civil Appeals Erred in Holding that Article 21.38, Section 2, Subsection (e) of the Texas Insurance Code is Unconstitutional as a Violation of Due Process, Section 19, Article I of the Texas Constitution.

POINT IV.

"The Court of Civil Appeals Erred in Failing to pass on and in Failing to Hold that Article 21.38, Section 2, Subsection (e) of the Texas Insurance Code is Constitutional and Not a Violation of the Equality and Uniformity Clauses of the Texas Constitution, Sections 1 and 2, Article VIII."

The Trial Court judgment did not specify the grounds of unconstitutionality supporting the judgment. The Court of Civil Appeals (R. 187) recognized the grounds to be:

> "It is the contention of appellee that Sec. 2(e), Art. 21.38, supra, is violative of the 'due process' clauses of the Constitution of the United States and Texas (Sec. 1, 14th Amendment, Art. 1, Sec. 19, respectively, Vernon's Ann. St.) and of the 'equality and uniformity' clause of the Texas Constitution (Secs. 1 and 2, Art. 8), and the equal protection clause of the United States Constitution (Sec. 1, 14th Amendment)."

Although the Texas Supreme Court stated in a per curiam opinion that the case was controlled by *St. Louis Cotton Compress*, 260 U.S. 346, the court, nevertheless, refused the writ with the notation "No Reversible Error" (R. 242).

The refusal with the notation "No Reversible Error" means the Supreme Court recognizes that the Court of Civil Appeals has reached a correct result, but the Supreme Court does not necessarily approve the principle of law upon which the decision was based (The Federal Due Process Point). *Texas Rules of Civil Procedure No. 483, Texas Osage Cooperative Royalty Pool v. Clark*, 159 Tex. 441, 322 S.W. 2d 506; *Bridges v. City of Richardson*,

—Tex.—, —S.W. 2d— (decided Jan. 31. 1962). Therefore, the highest Texas court did not expressly approve the basis of decision in the Court of Civil Appeals and deliberately refused to limit the ground for the writ refusal to the federal questions.

On the other hand, an "unqualified" refusal of the writ would have approved the holding and opinion of the Court of Civil Appeals as a correct statement of the law and controlling principles, T.R.C.P. No. 483, *Agnew v. Coleman County Electric Coop.*, 153 Tex. 587, 272 S.W. 2d 877; *Bridges v. City of Richardson*, —Tex.— , —S.W.— 2d— (decided Jan. 31, 1962). Since the writ refusal was not "unqualified", the Court of Civil Appeals' opinion does not establish the grounds for the state judgment.

Petitioner's Point II in the Texas Supreme Court assigned as error the holding that the statute was unconstitutional under the Texas due process clause, and Point IV assigned as error the failure to hold the statute was not unconstitutional under the Texas Uniformity and Equality Clauses.

Petitioner's Point II admits the Court of Civil Appeals and the Trial Court holding is grounded on an adequate state ground, to-wit: Texas Due Process. Since the judgments in the appellate court simply affirm the trial court judgment which may have been based on adequate state grounds, the refusal of the Writ in the Texas Supreme Court may have also been on this adequate state ground.

Petitioner also admits the Texas and United States due process clauses are coextensive in the Application for Writ of Error (R. 195)

> "The Petitioners' first two points of error will be discussed here because, fundamentally, the same issues are involved. In this connection, it is observed that

> it has been held that Article I, Section 19 of the Texas Constitution restricts the powers of the Legislature to the same extent as the due process clause of Section 1 of the 14th Amendment of the United States Constitution. *Mellinger v. City of Houston*, 68 Tex. 37, 3 S.W. 239."

After admitting that the Texas and Federal Due Process clauses are coextensive, Petitioners could not now, in good grace, deny the Texas courts may have also held that Texas due process also condemns the tax.

The refusal with the notation "No Reversible Error" does not disclose the basis for refusal and does not negative the two adequate state grounds, but the notation deliberately announces the lower court opinion is not approved nor adopted. Thus, the refusal may have been based on adequate state ground, to-wit: (1) the Texas Due Process Clause or the Texas Equality and Uniformity Clauses.

The controlling jurisdictional principle is now well settled by *Durley v. Mayo*, 351 U.S. 277, as follows:

> "It is a well established principle of this Court that before we will review a decision of a state court it must *affirmatively appear* from the record that the federal question was presented to the highest court of the State having jurisdiction and that its decision of the federal question was necessary to its determination of the case . . . And where the decision of the state court *might* have been either on a state ground or on a federal ground and the state ground is sufficient to sustain the judgment, the Court will not undertake to review it" (Emphasis added)

This Court cannot know but may only guess as to the meaning of the notation, N.R.E. A guess, even though educated, is not a sufficient basis for the assumption of jurisdiction.

Since the Texas Supreme Court rendered no complete opinion and its judgment (Refusal of the Writ with the notation "No Reversible Error") *might* have also rested on the Texas Constitution's Due Process and Equality and Uniformity Clauses, this court should not take jurisdiction.

In *Stembridge v. Georgia*, 343 U.S. 541, the rule is stated:

> "We are without jurisdiction when the question of the existence of an adequate state ground is debatable."

Since (1) Petitioners assigned as error in the Texas Application for Writ an adverse holding on the Texas Due Process and Equality and Uniformity points, (2) the Texas Supreme Court carefully avoided limiting itself to one ground for refusal by the notation "No Reversible Error", and thereby also deliberately declined to limit itself to the grounds announced by the Court of Civil Appeals for affirmance, and (3) the affirmed Trial Court judgment does not specify a state or federal ground, the existence of an adequate state ground is clearly debatable.

The purpose of the Supreme Court's per curiam opinion (R 242) was to renounce the lower court's prophecy that *St. Louis Compress* would be overruled (R. 190-191) and to further admonish the lower Texas Court that prophecy belongs to the theologians and inspired poets rather than the judiciary. The purpose of the notation—N.R.E.—was probably to avoid limiting the refusal to the one federal ground specified in the opinion (R. 183-191).

The record does not affirmatively demonstrate that the Federal Due Process question was necessary to a determination of the case. The Texas decision may have been grounded on the Texas Due Process and Equality points, either of which is sufficient to sustain the judgment.

CONCLUSION

(1) The Texas unadmitted insurance tax should be held to be an unconstitutional violation of due process and equal protection

(2) *St. Louis Compress* should be reaffirmed.

(3) The state court judgment should be affirmed.

(4) Alternatively, the Petition for Certiorari should be dismissed for want of jurisdiction.

(5) Alternatively, the case should be remanded to the Texas courts for determination of the Texas Constitutional questions presented.

Respectfully submitted,

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CERTIFICATE OF SERVICE

A copy of this Brief for Respondent has been served pursuant to Supreme Court Rule No. 33 by depositing five copies of the Brief in a United States Mail Box, with first class postage prepaid, addressed to counsel of record for the Petitioner at his Post Office Address, Capitol Station, Austin 11, Texas.

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